RS650-2
2/14/89

JAPAN · ECONOMIC · INSTITUTE

JEI REPORT

A Two-Part Report: A and B

NO. 9B
March 3, 1989

IN THIS ISSUE:

House Panel Debates FSX Project 1

Japan Edges To Center Stage On LDC Debt 4

Foreign Aid Requests Soar 6

Japan-China Update 7

USTR To Review Telecommunications Trade Pacts With Japan 10

Notes: U.S.-Japan Free Trade Agreement; Plastic Injection Molding Machinery 11

House Panel Debates FSX Project

Japan's plan to coproduce with the United States a next-generation fighter support aircraft, FSX, again came under fire February 23 on Capitol Hill. Although the executive branch currently is in the midst of a three-week, interagency review of the bilateral accord -- due largely to criticism from Congress and certain administration policymakers that the longer-term economic implications of the project had not been assessed adequately -- congressional opponents appear bent on building a record that they hope ultimately will kill the deal. The FSX project, although defense-related, has become a lightning rod for a more widespread fear of declining U.S. competitiveness.

"This morning's hearing [is] on an innocent-sounding proposal that could be troubling as far as our long-range national security is concerned," stated Rep. James J. Florio, chairman of the House Energy and Commerce subcommittee on commerce, consumer protection and competitiveness. The New Jersey Democrat observed that while this would not be the first time the United States has worked closely with other nations, including Japan, on producing military aircraft,

In a new coordinated effort, the government and the private sector will establish the Japan International Development Organization at the end of March. JAIDO will help recycle Japanese funds to Third World development projects. An aid initiative still in the planning stages is the Global Infrastructure Fund, which envisions a broad base of public and private resources from both Japan and the United States. The fund would focus on developing large infrastructure projects in the Third World.

Meanwhile, Tokyo announced in mid-February its recognition of the current Burmese government and its lifting of a ban on aid to Rangoon. Aid was suspended early last autumn after a coup in Burma resulted in government instability. Some aid previously committed to Rangoon will be disbursed now, but Tokyo has not yet decided about future appropriations to the troubled country.

Japan is showing its commitment to expanded international assistance not just in allocating extra money but in looking for new and more effective ways to implement aid programs. In addition to the new government and private sector initiatives, Tokyo is expressing an interest in taking on more responsibility within multilateral aid agencies, such as the International Monetary Fund and the World Bank. World Bank President Barber Conable indicated in mid-February that the major members of the bank would be receptive to a larger Japanese role. Those seeking aid at the emperor's funeral already may have given Tokyo their informal acknowledgement of its new clout.

Gretchen Green

Japan-China Update

After several years of sharp swings, Sino-Japanese relations seem to have reached a more mature balance that is enabling new mutual opportunities. Trade relations, in particular, have improved from the turbulence of the mid-1980s. Both sides have taken or are planning steps to improve the trade and investment atmosphere that is the bedrock of sound relations. The two Asian giants are taking advantage of the positive trade tone to expand political and foreign policy ties. If common ground can be developed, the China-Japan combination could be a potent force for peace and stability in all of Asia.

In the past two years trade across the Sea of Japan has settled down from its overheated state of the mid-1980s when Japanese exporters and Chinese importers took maximum advantage of Beijing's economic policy of opening to the West. Japan's exports to China more than doubled between 1983 and 1985, while imports rose "only" about 28 percent (see Table). The rapid expansion of exports tilted the bilateral trade balance strongly in Japan's favor -- so strongly that it became a point of tension. Steps by Beijing to restrict Japanese imports, the liberalization of Japanese markets and the rising value of the yen against the Chinese yuan played a large role in quickly righting the imbalance. Since mid-1988 several other developments with important trade implications have occurred:

- The Coordinating Committee for Multilateral Export Controls, a Western group that regulates the flow of high technology goods to communist countries, significantly relaxed its restrictions on exports to China in July 1988 in the following areas: general-purpose mainframe computers for commercial use, computers for medical use, personal computers, optical-fiber communications equipment (including semiconductor laser components), and two types of

Japan's Trade with China, 1984-88

(in millions and percent change)

a. in yen

Year	Exports Value	Exports Change	Imports Value	Imports Change	Balance Value	Balance Change
1984	Y1,720,803	47.4%	Y1,411,271	16.7%	Y309,532	*
1985	2,991,151	73.8	1,552,365	10.0	1,438,786	364.8%
1986	1,666,511	-44.3	965,839	-37.8	700,672	-51.3
1987	1,198,213	-28.1	1,075,383	11.3	122,830	-82.5
1988	1,213,908	1.3	1,263,452	17.5	-49,544	-140.3

b. in dollars

Year	Exports Value	Exports Change	Imports Value	Imports Change	Balance Value	Balance Change
1984	$7,216.7	46.9%	$5,957.6	17.1%	$1,259.1	*
1985	12,477.4	72.9	6,482.7	8.8	5,994.7	376.1%
1986	9,856.2	-21.0	5,652.4	-12.8	4,203.8	-29.9
1987	8,249.8	-16.3	7,401.4	30.9	848.4	-79.8
1988	9,475.7	14.9	9,852.8	33.1	-377.1	-144.4

*Meaningless.

Source: Japan Tariff Association

semiconductor production equipment. The relaxation reinvigorated bilateral trade that had been frozen by the fallout from the mid-1987 disclosure that Toshiba Machine Tool Co., Ltd. had exported defense-related equipment to the Soviet Union.

• Beginning in October Beijing cracked down on the multitude of tiny foreign trade corporations that focused on luxury goods or that conducted unethical trade practices, such as illegal monopolization or price gouging. These "briefcase" companies were competing fiercely for choice domestic export goods (spurring inflation) and bringing in imports that did not contribute to China's economic modernization program (wasting scarce foreign exchange reserves). These small operations also were an expression of government corruption in many cases. The crackdown will help restore order to China's foreign trade.

• Also in October Beijing pledged to give priority consideration to joint venture applications for the development of energy resources, telecommunications networks, ports and raw materials. Approval of joint ventures involving investments of less than $30 million will be a local government responsibility. Approval of larger ventures will remain a prerogative of the central government. The power to appoint a joint venture's directors was taken away from Chinese bureaucrats and given to the joint venture partners. In addition, rules were altered to drop the 50-year limit on the duration of joint ventures. The changes also are expected to halve the 90-day approval time.

Despite these improvements, Japanese firms still encounter barriers to expanding trade. Exports of many items, such as cars, consumer electronics and high technology equipment, remain restricted either by Beijing for balance of payments reasons or by Tokyo for security reasons. The yen's appreciation also has given American and European competitors an edge in the Chinese market. Many trading companies have shifted to promoting imports of Chinese goods to Japan only to run into another set of problems. China often cannot fulfill its end of an export contract because of raw material shortages, poor quality and transportation inadequacies.

Both Beijing and Tokyo hope a Sino-Japan investment protection pact also will lead eventually to greater bilateral trade. Under the August 1988 document Beijing agreed for the first time to provide national treatment in terms of labor and business regulations to Japanese investments. Although some Japanese businessmen remain skeptical about how the accord will be implemented, a string of investments has been announced by other Japanese companies since the signing. Mitsui & Co., Ltd. plans to set up a suit-making operation in Inner Mongolia; C. Itoh & Co., Ltd. opened at least two additional offices in China and plans others; Citizen Watch Co., Ltd. will produce watch parts in one of China's special economic zones; and Matsushita Electric Industrial Co., Ltd. will open a videocassette recorder plant in Beijing this spring. China's nascent aviation and space industries are other promising areas for Japanese investment.

Comparatively quiet trade relations have allowed Tokyo and Beijing to devote attention to other matters. The Japan-China 21st Century Committee, a joint advisory body, is becoming a forum for the relatively free exchange of viewpoints on sensitive issues, such as Japan's adherence to a "one-China" policy in dealing with Taiwan and its efforts to rewrite World War II histories in ways that many see as whitewashing Japanese aggression in China and other Asian countries. The sensitivity of this last issue was highlighted by a rapidly arranged meeting with Chinese Foreign Minister Qian Qichen after the funeral ceremony for the Showa Emperor. In the meeting Prime Minister Noboru Takeshita, who earlier had told the Diet that historians will be the judges of whether Japan acted aggressively in the war, clarified those remarks by acknowledging that on occasion Japan had been an aggressor.

Tokyo also is trying to find a solution to the problem of Chinese student immigration. Several hundred applications to study in Japan have been put on hold while Tokyo tries to develop ways to prevent visa violations by students who get full-time jobs in Japan. Chinese students complain that the delay is costing them lost enrollment fees or other financial hardships. There were nearly 13,000 Chinese students in Japan at the end of 1987. Tokyo is trying to deal with a tremendous upsurge in applications; nearly 36,000 were submitted last year from the Shanghai area alone. The Ministry of Justice has been cracking down on unauthorized foreign workers through tighter immigration controls and shows little sympathy to the student complaints.

Finally, there are signs that the two countries are trying to align themselves on regional foreign policy issues. In recent talks foreign ministers from both sides explored cooperative diplomacy aimed at defusing the Kampuchea situation. Tokyo expressed its support for the position taken by the Association of Southeast Asian Nations and Prince Norodom Sihanouk. Beijing

responded by reiterating its willingness to talk with Prince Sihanouk and through him to ASEAN. Moreover, Beijing and Tokyo have taken note of rapprochement efforts between North Korea and South Korea with positive comments. Both countries also are discussing the Soviet Union's efforts to improve its relations with Asian nations.

Jon Choy

USTR To Review Telecommunications Trade Pacts With Japan

Japan is not off the hook on telecommunications trade with the United States despite the Bush administration's decision to tag the European Community and South Korea "priority" countries for negotiations to improve market opportunities for American suppliers of telecommunications equipment and services and for sanctions if these discussions fail. U.S. Trade Representative Carla Hills also announced February 21 that her office would review implementation of two telecommunications trade agreements with Japan, the primary target of the tough telecommunications provisions of the 1988 Omnibus Trade and Competitiveness Act. Ironically, being put on the review list is not necessarily the lesser of two evils for Japan.

The European Community and South Korea, selected from a list of eight second-round candidates for priority status, have a year from March 23 to remove barriers to U.S. exports of telecommunications products and services. In West Germany and France, reportedly the two EC member countries of top concern to administration trade officials, these barriers include buy-national government procurement policies, discriminatory technical standards, closed-door standards-setting procedures, limits on the provision of value-added services and restrictions on foreign investment. U.S. trade negotiators will be zeroing in on the same barriers plus high tariffs in their talks with South Korea.

If the negotiations with Bonn, Paris and Seoul appear to be making substantial headway, the talks can be extended for two more years. At the end of that time Washington must decide whether the American telecommunications industry has gained roughly the same access to the markets of West Germany, France and South Korea as suppliers in those countries have to the U.S. market. If the answer is no, the president has the option of retaliating in order to win market access reciprocity for U.S. companies providing telecommunications equipment and services.

The Japan review is on a faster, potentially more dangerous track. By April 30 USTR must determine whether Japan has followed through on the extensive policy and regulatory changes it agreed to make during the 1985 MOSS (market-oriented, sector-selective) negotiations to ensure nondiscriminatory treatment of foreign companies in the deregulated domestic market for telecommunications products and services and whether Nippon Telegraph and Telephone Corp. has made good on its twice-renewed 1981 pledge to open its procurement process to foreign competition. The short deadline for assessing the effectiveness of these two market opening arrangements is an outgrowth of another requirement of the 1988 trade act -- that USTR review existing telecommunications trade agreements as part of its annual inventory of foreign trade barriers, due this year by April 30.